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BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Ex Parte 582 (Sub-No. 1)

Major Rail Consolidation Procedures

COMMENTS OF THE

TRANSPORTATION INTERMEDIARIES ASSOCIATION

Robert A. Voltmann
Executive Director and Chief Executive Officer
Transportation Intermediaries Association
3601 Eisenhower Ave.
Alexandria, Virginia 22304

By:
Nicholas J. DiMichael
Thompson Hine & Flory LLP
1920 N St. N.W.
Suite 800
Washington, D.C. 20036
(202) 263-4103

Attorney for the Transportation Intermediaries Association

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The Transportation Intermediaries Association ("TIA") respectfully submits these comments to the Surface Transportation Board ("STB") in response to the Advance Notice of Proposed Rulemaking ("ANPR") issued by the Board on March 31, 2000. TIA agrees with the Board that the agency's policies on mergers needs to be reevaluated in the context of a substantially-consolidated rail industry.[1] Rail customers need consistent and reliable rail transportation to deliver raw materials and pick up finished products on a predictable and timely basis. This means a rail transportation service that responds to customer needs. Unfortunately, many rail customers are not receiving consistent, reliable or fairly-priced rail transportation service because of a lack of competition in the rail industry. Thus, TIA believes that the Board needs to consider regulatory changes– both in its rules governing rail mergers and in its rules more generally – in order to affirmatively enhance, rather than simply preserve, competition.

I. Identity and Interest of the Transportation Intermediaries Association

TIA is the only organization representing transportation intermediaries of all disciplines operating in domestic and international commerce. The members of TIA include: intermodal marketing companies ("IMCs"), property brokers, international forwarders, non-vessel operating ocean common carriers ("NVOCCs"), domestic freight forwarders, air forwarders, perishable commodity brokers, and logistics management companies. TIA also provides management services for the American International Freight Association (AIFA), a leading organization of NVOCCs. AIFA is the U.S. member of FIATA, an international organization of more than 40,000 freight forwarders. The members of TIA are fiercely independent businesses that fully support a deregulated, open marketplace for both large and small consumers.

II. Rail Mergers, Rail Competition, and Intermodal Traffic: Why TIA Is Concerned

With respect to rail carriers, TIA members deal with and arrange for the intermodal transportation of goods. In particular, TIA's intermodal marketing company ("IMC") members consolidate shipments of goods within the United States moving to or from domestic and international points, and negotiate with rail carriers for the transportation of these goods by rail for one part of the intermodal move. TIA members, then, both sell their consolidation services to, and are customers of, the railroads, utilizing rail carriage for at least one part of the movement of goods from origin to destination.

By definition, the <u>goods</u> shipped by IMCs are not captive to the railroads – they can be transported either solely by truck, or intermodally. The Board may ask: why,

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[1] However, TIA does not believe that it was either necessary or lawful for the Board to impose a moratorium on all major rail mergers to accomplish this goal. TIA applauds, however, the Board's

then, is TIA concerned about rail merger policy? If rail carriers merge and subsequently attempt to impose monopoly pricing on the transportation of these goods, won't these goods simply move via other modes? Will not the potential loss of business discipline any anticompetitive behavior by the railroads against IMCs?

The answer to this question is a straightforward "no." The reason for this answer lies in structure of the intermodal / intermediary industry as it has evolved today.

Specifically, rail carriers currently have merged to such an extent that, with respect to IMCs, they have monopsony power: rail carriers have become large enough and few enough buyers of intermodal marketing company services to determine winners and losers in the industry, not on the basis of economic efficiency determined by the marketplace, but on the business priorities and goals of the rail carriers involved.

In a truly competitive rail marketplace, if a particular IMC were providing poor service, rail carriers would refuse to buy the services of that provider, and that IMC would rightly fail. Similarly, in a truly competitive rail marketplace, if IMCs in general were not offering value to the supply-chain, rail carriers could and would refuse to buy such services, and again, such behavior would be economically rational and justifiable. But in a truly competitive marketplace, a rail carrier could not arbitrarily erect barriers against, and decide to pick and choose among, certain categories of IMC providers, and offer to sell rail services to one category, and not to another. The fact that rail carriers can (and do) do so indicates both that the rail marketplace is not truly competitive, and that rail carriers are in fact exercising monopsony power.

The artificial "selection" of IMCs by monopsonistic rail carriers shows itself in a number of ways. For example, in October 1998, one of the only two western rail carriers

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determination to take a fresh look at its merger approach in light of its experience with past mergers.

decided that it was working with "too many" IMCs. The BNSF unilaterally raised its "requirements" for buying from a particular IMC from $500,000 to $5 million annually, thus forcing many small and mid-sized IMCs either to go out of business or to form consortiums in order to survive. TIA members report that BNSF's action caused an astounding <u>60% or more</u> of IMCs providing service to shippers (all small to medium IMCs) to merge, combine contracts, or lose access to the BNSF network. Similarly, NS, one of the only two eastern carriers, recently announced that it was unilaterally raising its "volume minimum" for IMCs from 250 units a year to 1,000, thus favoring large IMCs at the expense of smaller companies. In another area, major railroads' control of intermodal equipment – and their decision to provide such equipment to some and not to others – can (and does) determine who wins and who loses in the marketplace, not on the basis of economic efficiency, but on the wishes and desires of the rail provider of that equipment.

In its March 17 decision in Ex Parte No. 582, *Public Views on Major Rail Consolidations*, the decision which led directly to this proceeding, the Board noted that its current regulations were "not appropriate for addressing the broad concerns associated with reviewing business deals geared to produce two transcontinental railroads," slip op. at 2. Similarly, in its ANPR, the Board noted that its current rules were "not adequate for addressing the broad concerns associated with reviewing any proposals that . . would likely lead to just two large North American transcontinental railroads." ANPR, slip op. at 2. <u>But the Board must realize that for virtually all shippers, a rail duopoly is NOW a fact of life</u>. Specifically, <u>an IMC desiring to arrange for rail services as part of an intermodal movement from the western United States to any point in the country has only two railroads with which it can deal– a rail "duopoly" already exists for all except those</u>

very few points in the center of the nation served by more than two Class I rail carriers. The same is true for an IMC desiring to ship from the eastern United States to the west. Thus, the revision of the Board's merger and other rules so that they can be "geared" to an economy in which only two carriers are providing rail services is completely appropriate, and long overdue.

Accordingly, in order to prevent or at least minimize the possibility of the railroads' exercising monoposony power, the Board should determine to intensify and broaden rail-to-rail competition as much as possible, to minimize the likelihood of collusion between the few remaining carriers; to provide as much customer choice as possible; and to encourage economic efficiency and fairness.

III. The Board Retains Jurisdiction Over Rail Intermodal Freight

In *Improvement of TOFC/COFC Regulation*, 364 I.C.C. 731 (1981) and 3 I.C.C.2d 869 (1987), the Interstate Commerce Commission found that a competitive market for rail intermodal freight movements existed and that government regulation and oversight of those movements was not necessary. However, the Commission, and now the Board retains jurisdiction over rail intermodal movements. *G&T Terminal Packaging Co., Inc. v. Consolidated Rail Corporation,* 830 F.2d 1230 (3d Cir. 1987).

At the time of the ICC's decision, there were more than 40 Class I railroads and several hundred IMCs. Today, a rail duopoly exists and there are fewer than 70 IMCs now serving the market. While TIA is in no way advocating a return to regulation, it is advocating that the Board recognize the changed marketplace and the need for oversight to preserve competition and access.

IV. The Rules to be Reviewed and Changed Must Go Beyond the Regulations Promulgated Specifically for Rail Mergers

In the ANPR, the Board referred to its "merger rules" and defined such rules as the regulations found at 49 C.F.R. Part 1180.0–1180.9. ANPR, slip op. at 3, note 8. However, the serious issues raised by parties in Ex Parte 582 and highlighted by the STB require review of other regulations, and rules established through adjudication as well.

Specifically, if the Board is going to "affirmatively enhance," and not just preserve, competition, as the Board suggests in the ANPR, slip op. at 4, then it should act more broadly than simply in its "merger rules." For example, a requirement that a newly-merged carrier provide switching at an agreed-upon fee to all exclusively-served shippers located within or adjacent to terminal areas (suggested as one approach by the Board in its ANPR) would mean that only shippers served by the merged carrier would obtain the benefits of this competition, which would create distinctions between similarly-situated-shippers, depending upon whether they happened to be on the lines of the merged carriers or not. Thus, the Board needs to act both within and outside of its "merger rules" to provide for a truly competitive rail marketplace.

V. The Board Should Consider A Variety of Steps to Preserve and Increase Competition in the Rail Marketplace

In view of the above, the STB should consider a variety of revisions to its merger and other rules in order to preserve and increase competition in the rail marketplace.

A. <u>The Board Should Review Its "Unreasonable Practice" Jurisdiction to Prevent Uneconomic Practices by Monoposonistic Rail Carriers</u>

Under 49 U.S.C. §10702 and 10704, the Board has jurisdiction over the reasonableness of rates, charges, and "practices" of carriers. As rail carriers have merged, they have gotten so large and so few that the rules and practices that they employ can have a devastating impact on small entities such as IMCs that sell them their services. The Board should make clear, in the context of the contemplated revisions to its merger rules, that it will closely review the practices of merged carriers to be sure that they are not unreasonable. In particular, the Board should carefully review any "minimum volume" and other economic restrictions of carriers, such as contract minimums, bonding requirements, and equipment allocation, to insure that such requirements do not unreasonably discriminate against smaller economic players in the marketplace.

TIA believes that application of these reforms should be broadened to apply not just in merger settings, but for all carriers. Application of such rules would go far to forestall additional loss of competition and expand the availability of competitive rail intermodal service to shippers.

B. Preservation of Existing Gateways

In order to preserve even the existing level of competition in the routing of traffic, it is imperative for the Board to alter its merger rules to require any merging carriers to maintain "open" gateways. For example, if a point today is served by both CSX and NS, traffic moving from the west (even from a single-served point, such as solely on UP) can at least take advantage of competition between NS and CSX on the movement from the interchange to the competitively-served eastern point. Indeed, the Board's "contract exception" to its bottleneck rules recognizes that shippers at such a point receive the benefits of such competition. *Union Pacific Railroad Company v. STB*, 202 F.3d 337, 342 (D.C. Cir. 2000). However, if UP were to merge with CSX, the competition between NS and CSX for the eastern portion of the move beyond the UP interchange would be lost (as well as the shipper's right to challenge the rate under the "contract exception").

Thus, the Board must act to preserve the routing competition that now exists. This is going to mean not just preserving the physical ability to route traffic, but in preserving the economic ability as well: routes can be "closed" not just by flatly restricting routing, but by pricing the traffic over the monopoly segment of the joint line route to economically prevent diversion to the competitor at the gateway.

C. Revision of Bottleneck Rules

If the Board is to "preserve" competition, much less "affirmatively enhance" it, the Board must review its bottleneck rules. Under the current rules as articulated in the Board's two decisions in STB Docket No. 41242, *Central Power and Light Company v. Southern Pacific Railroad Company* and consolidated cases, decisions served December 31, 1996 and April 30, 1997, a shipper has no right to demand, and no right to challenge, any rate over a "bottleneck" if the bottleneck carrier can provide origin to destination service, unless the shipper brings and wins a competitive access case. Unfortunately, the agency's competitive access rules have been so narrowly construed that a complaining shipper has never won a single case.

In a future vertical merger (practically speaking, the only kind of merger remaining), shippers will lose whatever rights they have had to route traffic over competing carriers, since the vertically-merging carriers will obtain the ability to provide origin to destination service to and from points served by each of them. In other words, under the Board's bottleneck decisions, after a future vertical merger a shipper will have no right to route its traffic over currently-competitive routes, much less routes now closed but which could be competitive if the bottleneck rules were changed.

In its ANPR, the Board has suggested requiring merger applicants to offer, upon request, contracts for the competitive portion of joint-line routes when the joint-line partner has a bottleneck segment. ANPR, slip op. at 7. The Board also suggested that it might require merger applicants to provide a new through route at a reasonable interchange point whenever they control a bottleneck segment and the shipper has entered into a contract with another carrier for the competitive segment. Finally, the Board suggested revisions of the "one lump" theory to rail mergers.

TIA supports all of these approaches, and believes that they should be broadened to apply not just in merger settings, but for all carriers. Application of such rules would go far to forestall additional loss of competition through mergers, and restore competition in routing that has been lost in past mergers.

D. The Board Should Review Its Approach to Paper Barriers for the Efficient Operation of Short Line and Regional Carriers

In a world where there are only two carriers – the world that exists today in most parts of the country – the Board should be particularly careful to preserve and enhance all the present and potential rail competition that might be provided by non-Class I carriers. Thus, the Board needs to radically re-think its policy regarding so-called "paper barriers," often created at the inception of the formation of a Class III carrier, that prevent that Class III carrier from interchanging with any carrier other than its "parent" carrier.

While these barriers may have had a purpose to encourage the formation of Class III railroads, it is time to re-think such restrictions from both an economic and competitive perspective. From an economic perspective, the Board should be able to carefully evaluate, in a particular circumstance, whether the Class I parent has already received the reasonable economic benefit of this restriction, such that further continuation of the competitive restriction is not appropriate. From a competitive standpoint, the restrictions that may have been relatively harmless when there were many Class I carriers providing competitive service, become positively harmful in a world where only two Class I railroads predominate in any particular geographic area.

VI. Conclusion

TIA respectfully requests the Board to take the above views into account as it develops proposals for its Notice of Proposed Rulemaking in this proceeding.

Respectfully submitted,

Robert A. Voltmann
Executive Director and Chief Executive Officer
Transportation Intermediaries Association
3601 Eisenhower Ave.
Alexandria, Virginia 22304

By: Nicholas J. DiMichael
Nicholas J. DiMichael
Thompson Hine & Flory LLP
1920 N. St. N.W., Suite 800
Washington, D.C. 20036
Attorney for the Transportation Intermediaries Association

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Certificate of Service

I hereby certify that I have served the above Comments on all parties of record, as required by the Board's rules and its decision in this proceeding.